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Ms. Maia Bellon, Director
Washington State Department of Ecology
P.O. Box 47600
Olympia, WA 98504-7600

Re: Clean Fuel Discussion

Dear Director Bellon:

These comments are submitted today on behalf of Steve Clark, President of Genesee Fuel & Heating Co., Inc., in Seattle, on behalf of his company and his membership organization, Washington Oil Marketers Association; and Jon Lucich, Vice President of Veneer Chip Transport in Tacoma, and his membership organization, the Washington Trucking Association. We are writing today to express our concerns about the Clean Fuel Standard Discussion Document (the "Discussion Document"), which outlines a potentially damaging plan to increase costs and artificially induce demand for renewable fuels and alternative energy resources whose time may not yet have come.

Who We Are

Genesee Fuel & Heating Co. was established in 1929 and provides premium grade home heating oil, BioHeat and propane delivery services in the Seattle area. Genesee Fuel is a member of the Washington Oil Marketers Association ("WOMA"), a nonprofit trade association with 78 individual and corporate members that sell products and services that support the petroleum industry. WOMA members account for nearly 80% of all petroleum products sold in Washington State, including 68,000,000 gallons of heating oil to residential and industrial users. WOMA members also employ over 10,000 people in the State of Washington.

Veneer Chip Transport is a family-owned and operated company established in 1946 that provides freight carriage service, including transport of wood residuals and other materials. Veneer Chip employees 94 people on a full-time basis, including 79 drivers. The company consumed 1,056,211 gallons of motor fuel in 2014, and operates in Washington, Northern Idaho and Oregon. Veneer Chip is a member of the Washington Trucking Association ("WTA"), a nonprofit corporation established in 1922 by a group of truck owners that now represents all segments of Washington's trucking industry. It has over 1,000 members across the trucking

industry, including common carriers, private carriers, dump truckers, log truckers, movers, and intermodal carriers.

Genesee, Veneer and the associations of which they are members support the Department of Ecology ("DOE") and many of its initiatives to protect the environment and improve the quality of life for Washington state residents. We, and our fellow association members, pay taxes, obtain permits, and comply with a wide range of environmental and other regulations. We use, sell and/or transport alternative fuels and participate in energy conservation and efficiency initiatives. Many of our employees and associates live and work in Washington State, where all of us are proud of the natural beauty of our surroundings and abundance of our natural resources. Where the costs of environmental protection programs make sense, or where critical environmental protection objectives are served, we support DOE and its mission.

DOE's low-carbon fuels standard ("LCFS") program, as described in the Discussion Document, raises serious concerns for us and fellow members in our organizations. LCFS would require regulated entities (fuel suppliers in Washington) to supply higher-cost fuels to Washington residents than they are prepared to pay for, in a misguided and ineffective effort to reduce carbon dioxide emissions per unit of fuel consumed. If DOE implements LCFS in the manner described in the Discussion Document (which itself borrows heavily from California's LCFS), DOE would need to regulate energy markets through a complex program that will unnecessarily increase costs for Washington consumers, generate an enormous bureaucratic burden, and yield little, or no real, sustainable reduction in climate change or its effects in the State of Washington.

LCFS Background

LCFS programs, as adopted in California and under development in Oregon, are enormously complicated programs intended to reduce the "carbon intensity" of the aggregate fuel mix within a particular jurisdiction. Under such a program, DOE would establish a carbon intensity goal–let's say a ten percent reduction in carbon intensity over a fixed period of time–let's say ten years. Regulated entities would need to ensure that the mix of fuels that they sell to their consumers comply with the carbon intensity goal for a particular year in question, or else purchase "credits" from entities that utilize alternative energy fuels or technologies.

Carbon intensity is the amount of greenhouse gas (carbon dioxide, mostly) emitted per unit of energy. It would be calculated for different fuels and technologies on the basis of "life cycle" emissions associated with different fuel production and delivery pathways. Conventional (petroleum-based) fuels would be relatively carbon-intense, and alternatives such as natural gas, electricity from specific non-carbon-intense sources and unconventional technologies would be awarded a lower carbon intensity score by DOE. The program would operate through the

creation and exchange of regulatory "credits." DOE would require suppliers of conventional fuels to purchase credits from suppliers of fuels that DOE deems to be preferable (less carbon-intense), such as ethanol, or unconventional technologies, such as battery-powered automobiles.

In simple terms, the program "works" by adding artificial regulatory costs to the cost of conventional petroleum fuels, which cost increase theoretically reduces demand for the conventional fuels. The added cost would be incurred by fuel suppliers buying credits from suppliers of alternative fuels and technologies. The revenues derived from the sale of credits would effectively subsidize unconventional fuels or technologies, and reduce their net consumer cost, thus driving up demand (in theory). By driving up the price of conventional fuels high enough, and providing enough of a subsidy for unconventional fuels or technologies, DOE hopes to change consumers' demand for different types of fuels and technologies. If successful, the net changes in demand would lower the average carbon intensity of fuels used in Washington.

Problems with LCFS

There are several objectionable aspects of this type of program.

***Higher Costs***. First, such programs (intentionally) increase the costs of conventional fuels. By requiring distributors and suppliers of conventional fuels to purchase credits representing lower-carbon fuels, the state adds a regulatory cost to conventional fuel prices. The impacts of these costs are not easy to calculate or predict, against the background of already highly volatile markets, but estimates range from ten cents per gallon to well over $1 per gallon.

The raw per-gallon cost increases understate the problem. By reducing the carbon intensity of fuels, on average, the state would also incidentally reduce the average energy content per gallon, resulting in more gallons being consumed for the same output (in the case of a vehicle driver, miles driven). Overall, the number of gallons consumed would have to increase to accomplish program goals. The cost increase includes the direct costs of increased costs per gallon, and the indirect costs of higher consumption, due to reduced energy content per gallon of alternative fuel.

These costs do not count the administrative burden of an LCFS program. Properly run, such a program requires governmental monitoring of all energy inputs and outputs in the state, and requires tracking and monitoring of all fuel purchases and transfers. The administrative and bureaucratic burden – both on the regulated community and on governmental resources – would be enormous. Although much of the cost would be borne internally by regulated entities (and added to the cost of fuel), there would need to be additional tax revenues available or some other

source of funding to cover the increase in DOE's staffing and budget necessary to manage Washington's energy economy. Based on the California experience with cap-and-trade, the additional government funding for administering the program could be expected to exceed tens of millions of dollars, or 5-10% of the overall program's cost to the economy.

***Picking Winners and Losers***. Second, these programs put the government in the role of picking winners and losers. Not all lower-carbon intensity fuels and technologies are economically competitive. If they were economically competitive, then they naturally would be used, and would not need to be subsidized to succeed. Many such alternative fuels and technologies are gaining market share as a result of falling prices and consumer demand. But under a LCFS, DOE and not the market would select fuels and technologies to be subsidized. DOE would review applications and determine whether the alternative fuels and technologies are eligible to generate credits in the LCFS, using a complex calculus of carbon intensity and other factors. DOE would, in effect, be deciding which fuels and technologies would be entitled to benefit from cross-industry subsidies on the basis of its objectives. In other words, DOE would decide which alternative technologies are viable, and which are not, instead of consumer demand.

***Government Management of Complex Markets***. Third, LCFS programs put governmental agencies into the role of micromanaging complex markets. To make the programs work, governmental agencies must calculate and fine tune the determinations of carbon intensity, based upon the location of production, the routes traveled to deliver the fuels, and the impact upon land use (among other things) of the production processes. These determinations are by no means objective, and they are not tasks for which government agencies are well suited. The result is a market driven by governmental calculations of average costs and benefits, a notion that is entirely inconsistent with a market driven by competition and consumer demand.

But more importantly, the viability of the entire concept–of the "market" for alternative fuels and the credits they can generate–depends upon the ability of DOE to predict the market for these alternative fuels and technologies. Even ethanol producers must have customers, and if DOE intends to use electric cars as an alternative credit-generating technology, then there must be people to buy them, use them or drive them. Without markets for the alternative fuels and technologies, the "credits" won't be available and the conventional fuel suppliers won't be able to purchase credits. If the government miscalculates, then either no credits will be available, or the prices at which such credits are available will be exorbitant.

The essential problem is this: LCFS programs do not directly regulate consumer demand, but instead regulate suppliers. Suppliers, as the regulated entities, would be out of compliance and could be penalized if too few consumers elect to buy alternative fuels or use alternative technologies. If the expected consumer demand for the alternative, lower-carbon fuels and

technologies does not materialize, then there will be a "shortage" of credits with which to achieve compliance. In that case, the prices of credits would soar, and could trigger shortages of conventional fuels. In California, a shortage of credits did materialize, driving regulators to propose "capping" the price of credits, which in turn would depress development of alternatives that generate credits, as market forces fail to generate sufficient alternative fuel credits.

Properly calibrating and managing this "market" for the exchange of credits is difficult and tricky, and threatens to upset the conventional fuels market as well as create huge incentives for untested or unworkable alternatives. This market also depends for its success upon a governmental agency successfully predicting consumer demand, or adjusting the market incentives to avoid unwelcome outcomes. The management of real-world markets is not a role at which DOE is experienced, and is not a role that we believe governmental agencies can successfully play.

***Insignificant Effect on Climate Change***. Fourth, the issue of greatest concern is that the program is unlikely to significantly affect emissions of carbon dioxide or climate change. If the program is completely successful, it would reduce average "carbon intensity" by around ten percent. This is not a ten percent reduction in emissions, but a ten percent reduction in greenhouse gas emissions per unit of energy. There would be no cap on the energy consumed, no cap on use and no cap on emissions. Unless the program harms Washington's economy, ordinary economic growth and population growth are likely to eliminate any actual reduction in greenhouse gas emissions. So, a reasonably likely scenario is maintaining present greenhouse gas emissions, but at enormous cost.

And then there is the concern that is obvious to anyone who thinks more broadly about the world outside of Washington's borders. Without a global agreement on greenhouse gas emissions, a reduction in Washington (the cost of which would be borne solely by Washington residents) would have no measurable effect on global greenhouse gas emissions or concentrations. In all likelihood, one new power plant built in China would equal or exceed the reductions, if any, in greenhouse gas emissions in Washington. Unless there is global consensus on a plan to share the costs of greenhouse gas emission reductions, those reductions are unlikely to occur, regardless of the level of additional cost DOE forces Washington residents to pay.

A similar problem arises because of the national regulation of interstate commerce in the United States. Under the U.S. Constitution, one state cannot regulate the citizens of other states or impermissibly burden interstate commerce. So a state acting alone, like Washington, cannot effectively prevent substitution of fuels in multi-state markets. If Washington adopts a LCFS, suppliers of fuels can simply substitute deliveries of conventional fuels in that state with unconventional fuels, and redirect the conventional fuels to consumers in other states who would

be happy to receive the lower-cost conventional fuels. If suppliers can make money in Washington by selling higher-priced alternative fuels there, they will do so, and will sell the conventional fuels in other states for the same prices that they would have received in Washington. Suppliers of alternative fuels win; Washington businesses and consumers lose.

Legal Authority

The legal foundation for an LCFS program in Washington is uncertain. Such a program is administrative, and requires statutory authorization by the legislature. An executive order cannot provide a sufficient basis for regulations that would rearrange a state-wide economy. Likewise, statutes aimed at reducing air pollutants to protect health cannot legitimately be used to justify massive rearrangements of Washington's economy, as the LCFS would require. New legislation would be needed to support and authorize such a program.

But even if there were new legislation, DOE is constrained by the federal Clean Air Act, which reserves to the U.S. Environmental Protection Agency ("EPA") the exclusive authority to regulate fuels and fuel additives, excluding California. California adopted separate legislation to support its LCFS, and is authorized by the Clean Air Act to do so (due to its pre-Clean Air Act regulatory programs). But Washington enjoys no such exemption, and is expressly precluded from such regulation. In order to adopt an LCFS, Washington would not only need new state legislation, but depending on how the program is structured, may need federal amendments to the Clean Air Act. EPA is already in the process of regulating the greenhouse gas emissions from vehicles, and already imposes renewable fuel standards, both of which already apply or will apply in Washington State. There does not seem to be a compelling reason for DOE or the state of Washington to propose or adopt potentially duplicative or conflicting programs.

Conclusion

LCFS, if adopted and enforced in Washington, will increase costs for us and for our association members. The costs are difficult to precisely quantify, but they will be significant. Such costs will be passed along to consumers, wherever possible, and where not possible, would force our companies and our members to change their businesses radically, or even stop operating. LCFS would therefore alter Washington's economy in ways that cannot be anticipated.

At the same time, the benefits of an LCFS program are unclear. The primary beneficiaries would appear to be individuals and companies that successfully earn DOE's approval, and are able to maximize their revenues from alternative fuels and technologies. Or, perhaps out-of-state fuel suppliers and consumers will benefit, as high-cost alternatives are provided within Washington, and lower-cost conventional fuels are diverted to other states and their residents. Although the

impact of DOE's proposed LCFS upon climate change is likely to be immeasurably small and impossible to accurately predict, the negative impacts upon Washington's economy are knowable and likely significant.

We urge DOE to abandon its proposal to pursue a LCFS program.

Very truly yours,

Rob McKenna

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